

Liquidity Management Centre B.S.C. (c)
CONSOLIDATED FINANCIAL STATEMENTS
31 DECEMBER 2006

INDEPENDENT AUDITORS' REPORT TO THE SHAREHOLDERS OF LIQUIDITY MANAGEMENT CENTRE B.S.C. (c)

We have audited the accompanying consolidated financial statements of Liquidity Management Centre B.S.C. (c) ['the Bank'] and its subsidiary ['the Group'] which comprise the consolidated balance sheet as at 31 December 2006 and the consolidated statement of income, consolidated statement of cash flows and consolidated statement of changes in equity for the year then ended, and a summary of significant accounting policies and other explanatory notes.

Board of Directors' Responsibility for the Financial Statements

The Board of Directors is responsible for the preparation and fair presentation of these consolidated financial statements in accordance with both the Financial Accounting Standards issued by the Accounting and Auditing Organisation for Islamic Financial Institutions, to operate in accordance with Islamic Shari'a and International Financial Reporting Standards. This responsibility includes: designing, implementing and maintaining internal controls relevant to the preparation and fair presentation of consolidated financial statements that are free from material misstatement, whether due to fraud or error; selecting and applying appropriate accounting policies; and making accounting estimates that are reasonable in the circumstances. In addition the Board of Directors is responsible for the Group's undertaking to operate in accordance with Islamic Shari'a Rules and Principles.

Auditors' Responsibility

Our responsibility is to express an opinion on these consolidated financial statements based on our audit. We conducted our audit in accordance with both International Standards on Auditing and Auditing Standards for Islamic Financial Institutions. Those standards require that we comply with the relevant ethical requirements and plan and perform the audit to obtain reasonable assurance whether the consolidated financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on the auditors' judgement, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal controls relevant to the entity's preparation and fair presentation of the consolidated financial statements in order to design audit procedures that are appropriate for the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal controls. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by Board of Directors, as well as evaluating the overall presentation of the consolidated financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

**INDEPENDENT AUDITORS' REPORT TO THE SHAREHOLDERS OF
LIQUIDITY MANAGEMENT CENTRE B.S.C. (c)
(Continued)**

Opinion

In our opinion, the consolidated financial statements present fairly, in all material respects, the financial position of the Group as of 31 December 2006 and of its financial performance and its cash flows for the year then ended in accordance with Financial Accounting Standards issued by the Accounting and Auditing Organization for Islamic Financial Institutions and Shari'a rules and principles as determined by the Shari'a Supervisory Board of the Group.

In addition, in our opinion, the consolidated financial statements present fairly, in all material respects, the financial position of the Group as of 31 December 2006 and of its financial performance and its cash flows for the year then ended in accordance with International Financial Reporting Standards.

Other Regulatory Matters

We confirm that, in our opinion, proper accounting records have been kept by the Bank and the consolidated financial statements, and the contents of the report of the Board of Directors relating to these consolidated financial statements, are in agreement therewith. We further report, to the best of our knowledge and belief, that no violations of the Bahrain Commercial Companies Law, nor of the Central Bank of Bahrain and Financial Institution Law, nor of the memorandum and articles of association of the Bank, have occurred during the year ended 31 December 2006 that might have had a material adverse effect on the business of the Bank or on its consolidated financial position and that the Bank has complied with the terms of its banking licence.

31 January 2007

Manama, Kingdom of Bahrain

Liquidity Management Centre B.S.C. (c)

CONSOLIDATED BALANCE SHEET

31 December 2006

	<i>Notes</i>	2006 <i>US\$ 000's</i>	<i>2005</i> <i>US\$ 000's</i>
ASSETS			
Cash and balances with bank		403	150
Murabaha receivables	3	30,322	14,140
Investments	4	181,198	88,146
Investment properties		4,906	-
Other assets	5	3,141	2,785
Fixed assets		141	132
TOTAL ASSETS		220,111	105,353
LIABILITIES AND EQUITY			
LIABILITIES			
Due to Sukukholders	6	158,352	82,468
Other liabilities	7	3,749	809
		162,101	83,277
EQUITY			
Share capital	9	51,000	20,000
Reserves	9	7,010	2,076
		58,010	22,076
TOTAL LIABILITIES AND EQUITY		220,111	105,353

The consolidated financial statements have been authorised for issue by the Board of Directors on
and signed on their behalf by:

Aref Ahmed Al-Kooheji
Chairman

Emad Al Monayea
Managing Director

Ahmed Abbas
Chief Executive Officer

The attached explanatory notes 1 to 17 form part of these consolidated financial statements.

Liquidity Management Centre B.S.C. (c)

CONSOLIDATED STATEMENT OF INCOME

Year ended 31 December 2006

	2006	2005
	<i>US\$ 000's</i>	<i>US\$ 000's</i>
Income from investments	7,731	3,379
Less: Return to Sukukholders	(6,397)	(2,490)
	1,334	889
Income from Murabaha receivables	967	333
Fees (note 8)	6,842	2,400
(Loss)/gain on investment carried at fair value through statement of income	(479)	743
Gain on sale of investments carried at amortised cost	238	30
Other income	26	20
OPERATING INCOME	8,928	4,415
Staff costs	2,324	1,781
Depreciation	68	53
General and administrative expenses	443	490
OPERATING EXPENSES	2,835	2,324
NET PROFIT FOR THE YEAR	6,093	2,091

The attached explanatory notes 1 to 17 form part of these consolidated financial statements.

Liquidity Management Centre B.S.C. (c)

CONSOLIDATED STATEMENT OF CASH FLOWS

Year ended 31 December 2006

	2006 US\$ 000's	2005 US\$ 000's
OPERATING ACTIVITIES		
Net profit for the year	6,093	2,091
Adjustment for:		
Depreciation	68	53
Amortisation of premium on investments	(16)	5
Loss/(gain) on investments carried at fair value through statement of income	479	(743)
Gain on sale of investments carried at amortised cost	(238)	(30)
Operating profit before working capital changes	<u>6,386</u>	<u>1,376</u>
Changes in:		
Murabaha receivables	(7,313)	-
Other assets	(356)	(1,464)
Other liabilities	2,940	394
Net cash from operating activities	<u>1,657</u>	<u>306</u>
INVESTING ACTIVITIES		
Purchase of investment carried at fair value through statement of income	(47)	(48)
Purchase of investments carried at amortised cost	(102,123)	(66,444)
Sale proceeds of investments carried at amortised cost	8,894	18,326
Purchase of investment property	(4,906)	-
Purchase of fixed assets	(77)	(43)
Net cash used in investing activities	<u>(98,259)</u>	<u>(48,209)</u>
FINANCING ACTIVITIES		
Sukuk issue	75,884	46,921
Directors' remuneration paid	(160)	-
Increase in share capital (note 9)	30,000	-
Net cash from financing activities	<u>105,724</u>	<u>46,921</u>
INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	9,122	(982)
Cash and cash equivalents at 1 January	<u>14,290</u>	<u>15,272</u>
CASH AND CASH EQUIVALENTS AT 31 DECEMBER	<u>23,412</u>	<u>14,290</u>
Cash and cash equivalents at year end comprise of:		
Cash and balances with bank	403	150
Murabaha receivables maturing within ninety days	23,009	14,140
	<u>23,412</u>	<u>14,290</u>

The attached explanatory notes 1 to 17 form part of these consolidated financial statements.

Liquidity Management Centre B.S.C. (c)

CONSOLIDATED STATEMENT OF CHANGES IN EQUITY

Year ended 31 December 2006

	<i>Reserves</i>						<i>Total equity</i> US\$ 000's
	<i>Share capital</i> US\$ 000's	<i>Statutory reserve</i> US\$ 000's	<i>General reserves</i> US\$ 000's	<i>Investment fair value reserve</i> US\$ 000's	<i>Retained earnings</i> US\$ 000's	<i>Total Reserves</i> US\$ 000's	
Balance at 1 January 2006	20,000	209	209	154	1,504	2,076	22,076
Cumulative changes in fair value	-	-	-	1	-	1	1
Transfer of fair value gain to reserve, net	-	-	-	264	(264)	-	-
<i>Income recognised directly in equity</i>	-	-	-	265	(264)	1	1
Net profit for the year	-	-	-	-	6,093	6,093	6,093
<i>Total income and expenses recognised during the year</i>	-	-	-	265	5,829	6,094	6,094
Increase in share capital (note 9)	30,000	-	-	-	-	-	30,000
Bonus shares issued (note 9)	1,000	-	-	-	(1,000)	(1,000)	-
Directors' remuneration paid	-	-	-	-	(160)	(160)	(160)
Transfer to statutory reserve	-	609	-	-	(609)	-	-
Transfer to general reserve	-	-	609	-	(609)	-	-
Balance at 31 December 2006	51,000	818	818	419	4,955	7,010	58,010
Balance at 1 January 2005	20,000	-	-	189	(169)	20	20,020
Cumulative changes in fair value	-	-	-	(35)	-	(35)	(35)
<i>Income recognised directly in equity</i>	-	-	-	(35)	-	(35)	(35)
Net profit for the year	-	-	-	-	2,091	2,091	2,091
<i>Total income and expenses recognised during the year</i>	-	-	-	(35)	2,091	2,056	2,056
Transfer to statutory reserve	-	209	-	-	(209)	-	-
Transfer to general reserve	-	-	209	-	(209)	-	-
Balance at 31 December 2005	20,000	209	209	154	1,504	2,076	22,076

The attached explanatory notes 1 to 17 form part of these consolidated financial statements.

1 INCORPORATION AND ACTIVITIES

Liquidity Management Centre B.S.C. (c) (the "Bank") is a closed joint stock company incorporated in the Kingdom of Bahrain on 31 July 2002 and registered with Ministry of Industry and Commerce under commercial registration (CR) number 49092. The Bank operates in Bahrain under an investment banking license issued by the Central Bank of Bahrain (CBB). The Bank is engaged in the following activities:

- Facilitate creation of an Islamic inter-bank money market that will allow Islamic Financial Services Institutions ("IFSI") to effectively manage their assets and liabilities.
- Provide short-term liquid, tradable asset backed treasury instruments (Sukuk) based on Islamic Shari'a principles where IFSI can invest their surplus liquidity.
- Provide short-term investment opportunities based on Islamic Shari'a principles.

The activities of the Bank and its wholly owned subsidiary (the "Group") are to carry out operations in accordance with the teachings of Islam (Shari'a). The Group's Shari'a Supervisory Board is entrusted to ensure the Group's adherence to Shari'a rules and principles in its transactions and activities.

For the purpose of attainment of its investment objectives, the Group also sets up establishments or finance divisions or carries on such activities which include but not restricted to the following:

- i) Act as an agent for Special Purpose Vehicles ("SPV") established to securitise assets.
- ii) Establish SPVs of various kinds to carry on all the activities connected therewith.
- iii) Facilitate the sourcing and securitisation of assets, acquired from various sources.
- iv) Establish lines of liquidity to support the issuance of securitised instruments (Sukuk).
- v) Actively trade Sukuk by offering buy/sell quotes and service all investors in Sukuk.

The address of the Bank's registered office is Building 722, Road 1708, Block 317, Manama, Kingdom of Bahrain.

The Bank operates only in the Kingdom of Bahrain.

2.1 BASIS OF PREPARATION

The consolidated financial statements are prepared in accordance with International Financial Reporting Standards, Financial Accounting Standards issued by the Accounting and Auditing Organisation for Islamic Financial Institutions (AAOIFI), in conformity with the Bahrain Commercial Companies Law, Central Bank of Bahrain and Financial Institution Law. These consolidated financial statements are presented in US dollars, being the functional currency of the Group.

2.2 New and amended standards issued but not yet effective

The following standards and interpretations have been issued but are not yet effective.

- * IFRS 7 Financial instruments : Disclosures and consequent amendments to IAS 1 - Capital Disclosures
- * IFRS 8 Operating Segments

The above amendments only impact disclosures and will be effective for 2007 and 2009 respectively.

- * IFRIC Interpretation 8 Scope of IFRS 2
- * IFRIC Interpretation 11 IFRS 2 - Group and Treasury Share Transactions

Management do not expect these interpretations to have a significant impact on the Bank's financial statements when implemented in 2007.

2.3 BASIS OF ACCOUNTING CONVENTION

The consolidated financial statements have been prepared on historical cost basis, except for investment properties, available for sale investments and investments carried at fair value through statement of income, that have been measured at fair value.

2.4 SIGNIFICANT ACCOUNTING POLICIES

The accounting policies used in the preparation of these consolidated financial statements are consistent with those used in previous year.

Basis of consolidation

These consolidated financial statements incorporate the financial statements of the Bank and its wholly owned subsidiary "The Short Term Sukuk Centre B.S.C. (closed)" (STSC). A subsidiary is an entity over which the Bank has power to control, which is other than fiduciary in nature. The results of the subsidiary are included in the consolidated financial statements from the effective date of formation or acquisition. All intercompany balances and transactions, including unrealised profits arising from intra-group transactions, have been eliminated in full.

The financial statements of STSC are prepared for the same reporting year as the Bank using consistent accounting policies and adjustments have been made to bring into line any dissimilar accounting policies that may exist.

Murabaha receivables

Murabaha receivables are sales or credit terms, based on the delivery of a commodity, which is the subject of the Murabaha, by the seller to the buyer and enabling it to possess and benefit from the commodity, with the understanding that the buyer will pay the agreed price at a certain future date inclusive of a profit margin.

Receivable under murabaha contracts are stated net of provision for impairment if any, and deferred profits.

Investments

All investments are initially recognised at cost, being the fair value of the consideration given and including acquisition charges associated with the investments.

These are classified as follows:

- i) *Investments carried at fair value through statement of income*
After initial recognition, these are measured at fair value with any gain or loss arising from a change in fair value being included in the consolidated statement of income in the period in which it arises.

Since such investments would be classified as "available for sale" under AAOIFI, the unrealised gains arising from re-measurement to fair value are appropriated to investment fair value reserve and are transferred to retained earnings only when realised.

- ii) *Held to maturity*
Investments in Sukuk having fixed or determinable payments and fixed maturity where the Group has both the intent and the ability to hold such investments to maturity are classified as held to maturity. After initial recognition such investments are carried at amortised cost less provision for impairment in value. Amortised cost is calculated using the effective profit rate that takes into account the effect of any premium or discount on acquisition.

2.4 SIGNIFICANT ACCOUNTING POLICIES (continued)

Investments (continued)

iii) *Available for sale*

After initial recognition these investments are remeasured at fair value, unless fair value cannot be reliably measured. All changes in fair value of such assets subsequent to initial recognition are reported in the consolidated statement of equity and held in a reserve until realisation.

iv) *Investments carried at amortised cost*

Sukuk (debt instruments) which do not meet the definition of held to maturity and which have fixed or determinable payments but are not quoted in an active market are treated effectively as investments carried at amortised cost less provision for impairment in value.

Investment property

The Bank holds certain properties as investments to earn rental income, for capital appreciation, or both. Investment properties are measured initially at cost, including transaction costs. Subsequent to initial recognition, investment properties are stated at fair value, which reflects market conditions at the balance sheet date. Gains or losses arising from the changes in the fair values of investment properties are included in the consolidated statement of income in the year in which they arise.

In accordance with AAOIFI unrealised gains are appropriated to an investment fair value reserve and are transferred to retained earnings only when realised.

Financial instruments

Financial assets and financial liabilities carried on the balance sheet include cash and bank balances, murabaha receivables, investments, other assets, due to sukukholders and other liabilities.

Financial instruments are classified as liabilities or equity in accordance with the substance of the contractual arrangement. Profit, dividends, gains and losses relating to a financial instrument classified as a liability, are reported as expense. Distributions to holders of financial instruments classified as equity are charged directly to equity.

Fair value

The determination of fair value is done for each investment individually in accordance with the valuation policies set out below:

- (i) For investments quoted in an active market, fair value is determined by reference to quoted market prices.
- (ii) For acquisition made within one year of the reporting date, cost is assumed to be the fair value. For other investments, where there is no quoted market price, a reasonable estimate of the fair value is determined by reference to the current market value of another investment which is substantially the same, or is based on an assessment of the value of future cash flows.
- (iii) The fair value of investment property is based on external valuations.

Investments for which fair value cannot be determined as set out above, are carried at cost.

Derecognition

A financial asset (or, where applicable a part of a financial asset or part of a group of similar financial assets) is derecognised when:

2.4 SIGNIFICANT ACCOUNTING POLICIES (continued)

Derecognition (continued)

- (i) the right to receive cash flows from the asset have expired;
- (ii) the Bank retains the right to receive cash flows from the asset, but has assumed an obligation to pay them in full without material delay to a third party under a 'pass through' arrangement; or
- (iii) the Bank has transferred its rights to receive cash flows from the asset and either (a) has transferred substantially all the risks and rewards of the asset, or (b) has neither transferred nor retained substantially all the risks and rewards of the asset, but has transferred control of the asset.

When the Bank has transferred its rights to receive cash flows from an asset and has neither transferred nor retained substantially all the risks and rewards of the asset nor transferred control of the asset, the asset is recognised to the extent of the Bank's continuing involvement in the asset.

A financial liability is derecognised when the obligation specified in the contract is discharged, cancelled or expired.

Impairment and uncollectability of financial assets

An assessment is made at each balance sheet date to determine whether there is objective evidence that a specific financial asset may be impaired. If such evidence exists, the estimated recoverable amount of that asset is determined and any impairment loss, based on the assessment by the Bank of the value to it of anticipated future cash flows, is recognised in the consolidated statement of income. Specific provisions are created to reduce all impaired financial contracts to their expected realisable value.

For available for sale investments reversal of impairment losses are recorded as increases in cumulative changes in fair value through equity.

Sukuk assets under management

Sukuk assets managed in a fiduciary capacity are not treated as assets of the Bank and accordingly are not included in the consolidated balance sheet.

Revenue recognition

Income from investments

Income from investments is recognised on a time-apportioned basis over the period of investment. Income that is ninety days or more overdue is excluded from income until it is received in cash.

Income from Murabaha receivables

As the income is quantifiable and contractually determined at the commencement of the contract, the income is recognised on a time apportioned basis over the period of the contract based on the principal amounts outstanding and the profit rate agreed with customers. Income that is 90 days or more overdue is excluded from income.

Fees

These comprise fee for structuring, arranging and underwriting deals. Structuring and arranging fee income is recognised by reference to percentage of completion method, measured by reference to the percentage of cost incurred to date to estimated total cost. Underwriting and other fees are recognised when earned.

Return to Sukukholders

Return to Sukukholders is recognised in accordance with the underlying contracts.

2.4 SIGNIFICANT ACCOUNTING POLICIES (continued)

Offsetting

Financial assets and financial liabilities are only offset and the net amount reported in the balance sheet when there is a legally enforceable right to set off the recognised amounts and the Bank intends to either settle on a net basis, or to realise the asset and settle the liability simultaneously.

Foreign currencies

Foreign currency transactions are recorded in US dollars at rates of exchange ruling at the value dates of the transactions. Monetary assets and liabilities in foreign currency are retranslated into US dollars at the rates of exchange ruling at the date of balance sheet. Any resultant gains or losses are taken to income.

Non monetary items that are measured in terms of historical cost in a foreign currency are translated using the exchange rates as at the dates of the initial transactions. Translation gains or losses on non-monetary items carried at fair value (other than those carried at fair value through statement of income) are included in equity as part of the fair value adjustment on investments available for sale.

Judgements

In the process of applying the Group's accounting policies, management has made the following judgements, apart from those involving estimations, which have the most significant effect in the amounts recognised in the consolidated financial statements:

Classification of investments

Management decides on acquisition of an investment whether it should be classified as carried at fair value through statement of income, held to maturity, available for sale or investments carried at amortised cost.

Classification of investments as fair value through statement of income depends on how management monitors the performance of these investments.

For those deemed to be held to maturity management ensures that the requirements of IAS 39 are met and in particular the Group has the intention and ability to hold these to maturity.

The Group classifies debt instruments as carried at amortised cost if the debt instruments are not quoted in an active market.

All other investments are classified as available for sale.

Use of estimates in preparation of the consolidated financial statements

The preparation of the consolidated financial statements requires management to make estimates and assumptions that affect the reported amounts of financial assets and liabilities at the date of the financial statements. The assumptions are discussed below:

The determination of impairment provisions for available for sale investments. The valuation of such provisions is based on impairment criteria explained above.

The determination of fair values of unquoted investments. The valuation of such investments is based on fair value criteria explained above.

Cash and cash equivalents

Cash and cash equivalents comprise cash and balances with a bank and Murabaha balances maturing within ninety days from the acquisition date.

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2.4 SIGNIFICANT ACCOUNTING POLICIES (continued)**Zakah**

In accordance with its Articles of Association, the Bank is not required to pay Zakah on behalf of its shareholders.

Employees' end of service benefits

Provision is made for employees in accordance with the amounts payable under Bahrain Labour law applicable and the employment contracts based on accumulated periods of service at the date of balance sheet. Bahraini employees are also covered under the General Organisation for Social Insurance scheme.

3 MURABAHA RECEIVABLES

	<i>2006</i> <i>US\$ 000's</i>	<i>2005</i> <i>US\$ 000's</i>
International commodities Murabaha	30,322	14,140

The Bank considers the promise made by the purchase orderer in the Murabaha contract as obligatory. The effective profit return on these facilities as of 31 December 2006 ranged between 4.2% and 7.35% per annum (2005: 4.25% and 4.64% per annum).

The Murabaha receivables are considered as cash equivalents and include a significant portion which is with a related party in the normal course of business (note 10).

4 INVESTMENTS

	<i>2006</i> <i>US\$ 000's</i>	<i>2005</i> <i>US\$ 000's</i>
Investments carried at amortised cost	157,897	66,409
Held to maturity	14,666	14,671
Available for sale	8,103	6,102
Investments carried at fair value through statement of income	532	964
	181,198	88,146

The above investments are categorised as follows:

2006	<i>Face Value</i> <i>US\$ 000's</i>	<i>Carrying value</i> <i>US\$ 000's</i>
Quoted		
Banks and financial institutions	23,404	23,301
Governments	12,000	12,832
Corporate		
-Real Estate	78,293	75,280
-Construction and building materials	20,000	19,785
	133,697	131,198
Unquoted		
Corporate		
-Real Estate	50,000	50,000
Total	183,697	181,198

31 December 2006

4 INVESTMENTS (continued)

2005	<i>Face Value</i> <i>US\$ 000's</i>	<i>Carrying value</i> <i>US\$ 000's</i>
Quoted	78,066	78,146
Unquoted	10,000	10,000
Total	<u>88,066</u>	<u>88,146</u>

The above investments include an amount of US\$ 178 million representing the underlying assets of the secured Short Term Sukuk Program (STS Program) of The Short Term Sukuk Centre B.S.C. (c) managed by the Bank. The maturities range from 1 to 5 years and the effective profit rate on these investments ranged between 3.63% to 7.99% per annum (2005: 3.63% to 6.71% per annum).

5 OTHER ASSETS

	<i>2006</i> <i>US\$ 000's</i>	<i>2005</i> <i>US\$ 000's</i>
Accrued income receivable	2,737	2,217
Prepaid expenses	29	109
Others	375	459
	<u>3,141</u>	<u>2,785</u>

6 DUE TO SUKUKHOLDERS

Due to Sukukholders represent STS program Sukuk owned by the investors in the secured Short Term Sukuk Program (STS Program) of The Short Term Sukuk Centre B.S.C. (c) managed by the Bank. The investors are the legal owners of the underlying investments of US\$ 178 million of the STS program as disclosed in note 4. Returns paid to the Sukukholders during the year ranged between 4.39% and 5.85% per annum (2005: 2.57% to 4.5% per annum).

7 OTHER LIABILITIES

	<i>2006</i> <i>US\$ 000's</i>	<i>2005</i> <i>US\$ 000's</i>
Staff related payables	1,138	648
Fees payable	2,121	-
Others	490	161
	<u>3,749</u>	<u>809</u>

8 FEES

	<i>2006</i> <i>US\$ 000's</i>	<i>2005</i> <i>US\$ 000's</i>
Structuring and arranging	5,026	2,139
Underwriting	1,816	261
	<u>6,842</u>	<u>2,400</u>

31 December 2006

9 EQUITY**(i) Share capital**

	<i>2006</i> <i>US\$ 000's</i>	<i>2005</i> <i>US\$ 000's</i>
Authorised		
200 ordinary shares of US\$1,000,000 each	200,000	200,000
Issued, subscribed and fully paid		
20 ordinary shares of US\$1,000,000 each	20,000	20,000
Increase in share capital *	31,000	-
	51,000	20,000

* At the Extraordinary General Meeting held on 7 December 2006, the shareholders of the Bank approved changes to the memorandum and articles of associations for an increase of US\$ 31 million in paid-up share capital as follows:

- US\$ 30 million by way of issuance of right shares.
- US\$ 1 million by way of issuance of bonus shares.

The Bank is in the process of updating the memorandum and articles of association to incorporate the above capital increase.

(ii) Statutory reserve

In accordance with the requirements of the Bahrain Commercial Companies Law, 10% of the net profit for the year has been transferred to a statutory reserve. The Bank may resolve to discontinue such annual transfers when the reserve total 50% of the paid up share capital. The reserve is not distributable but can be utilised for the purpose of a distribution in such circumstances as stipulated in the Bahrain Commercial Companies Law and with the prior approval of the CBB.

(iii) Investment fair value reserve

Investment fair value reserve represents unrealised gains resulting from re-measurement of available-for-sale investment and unrealised revaluation gains on investment carried at fair value through statement of income, as required by AAOIFI. This reserve is distributable upon value realisation, which takes place at the time of actual exit or derecognition.

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10 RELATED PARTY TRANSACTIONS

The Group enters into transactions with its shareholders, directors, senior management and their related concerns in the ordinary course of business on commercial terms. All the financing transactions with related parties are performing and are free of provisions for possible impairment.

The balances of major transactions with related parties which mainly comprises major shareholders are as follows:

	<i>2006</i>	<i>2005</i>
	<i>US\$ 000's</i>	<i>US\$ 000's</i>
Cash and balances with bank	403	150
Murabaha receivables	12,611	9,472
Due to Sukukholders	100,462	54,016

The income and expenses arising from dealing with related parties comprises shareholders included in the consolidated statement of income are as follows:

	<i>2006</i>	<i>2005</i>
	<i>US\$ 000's</i>	<i>US\$ 000's</i>
Income from Murabaha receivables	514	186
Return to Sukukholders	3,599	1,367

Compensation of the key management personnel is as follows:

Short term employee benefits	706	571
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11 LIQUIDITY RISK

Liquidity risk is the risk that an institution will be unable to meet its net funding requirements. Liquidity risk can be caused by market disruptions or credit downgrades which may cause certain sources of funding to cease immediately. For STS Program the Bank manages liquidity risk by entering into liquidity support agreements with other financial institutions.

The contractual maturities of assets and liabilities have been determined on the basis of the remaining period at the date of the balance sheet to the contractual maturity date. The maturity profile of the assets and liabilities at the year end are based on contractual repayment arrangements.

Liquidity Management Centre B.S.C. (c)

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

31 December 2006

11 LIQUIDITY RISK (continued)

The maturity profile of assets, liabilities and equity is as follows:

31 December 2006	<i>Up to 1 month US\$ 000's</i>	<i>1 to 3 months US\$ 000's</i>	<i>3 to 6 months US\$ 000's</i>	<i>6 months to 1 year US\$ 000's</i>	<i>1 to 3 years US\$ 000's</i>	<i>Over 3 years US\$ 000's</i>	<i>Undated US\$ 000's</i>	<i>Total US\$ 000's</i>
ASSETS								
Cash and balances with bank	403	-	-	-	-	-	-	403
Murabaha receivables	23,009	-	5,186	2,127	-	-	-	30,322
Investments	-	532	-	696	51,473	128,497	-	181,198
Investment properties	-	-	4,906	-	-	-	-	4,906
Other assets	359	320	2,446	-	-	-	16	3,141
Fixed assets	-	-	-	-	-	-	141	141
Total assets	<u>23,771</u>	<u>852</u>	<u>12,538</u>	<u>2,823</u>	<u>51,473</u>	<u>128,497</u>	<u>157</u>	<u>220,111</u>
LIABILITIES AND EQUITY								
Due to Sukukholders	158,352	-	-	-	-	-	-	158,352
Other liabilities	1,054	2,146	293	-	-	256	-	3,749
Equity	-	-	-	-	-	-	58,010	58,010
Total liabilities and equity	<u>159,406</u>	<u>2,146</u>	<u>293</u>	<u>-</u>	<u>-</u>	<u>256</u>	<u>58,010</u>	<u>220,111</u>
Liquidity gap	<u>(135,635)</u>	<u>(1,294)</u>	<u>12,245</u>	<u>2,823</u>	<u>51,473</u>	<u>128,241</u>	<u>(57,853)</u>	
Cumulative liquidity gap	<u>(135,635)</u>	<u>(136,929)</u>	<u>(124,684)</u>	<u>(121,861)</u>	<u>(70,388)</u>	<u>57,853</u>	<u>-</u>	

The net funding requirement with regards to cumulative liquidity gap are managed through liquidity lines amounting to US\$95 million provided by the shareholders (fully utilised).

Liquidity Management Centre B.S.C. (c)

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

31 December 2006

11 LIQUIDITY RISK (continued)

31 December 2005	<i>Up to 1 month US\$ 000's</i>	<i>1 to 3 months US\$ 000's</i>	<i>3 to 6 months US\$ 000's</i>	<i>6 months to 1 year US\$ 000's</i>	<i>1 to 3 years US\$ 000's</i>	<i>Over 3 years US\$ 000's</i>	<i>Undated US\$ 000's</i>	<i>Total US\$ 000's</i>
ASSETS								
Cash and balances with bank	150	-	-	-	-	-	-	150
Murabaha receivables	9,472	4,668	-	-	-	-	-	14,140
Investments	-	964	-	-	10,011	77,171	-	88,146
Other assets	568	1,059	1,142	-	-	-	16	2,785
Fixed assets	-	-	-	-	-	-	132	132
Total assets	10,190	6,691	1,142	-	10,011	77,171	148	105,353
LIABILITIES AND EQUITY								
Due to Sukukholders	82,468	-	-	-	-	-	-	82,468
Other liabilities	93	446	-	73	-	197	-	809
Equity	-	-	-	-	-	-	22,076	22,076
Total liabilities and equity	82,561	446	-	73	-	197	22,076	105,353
Liquidity gap	(72,371)	6,245	1,142	(73)	10,011	76,974	(21,928)	
Cumulative liquidity gap	(72,371)	(66,126)	(64,984)	(65,057)	(55,046)	21,928	-	

The net funding requirement with regards to cumulative liquidity gap are managed through liquidity lines amounting to US\$ 95 million provided by the shareholders (utilised US\$ 54 million).

12 CREDIT RISK AND CONCENTRATION OF ASSETS AND LIABILITIES

Credit risk is the risk that one party to a financial instrument will fail to discharge an obligation and cause the other party to incur a financial loss. The Group attempts to control credit risk by monitoring credit exposures, limiting transactions with specific counterparties, and continually assessing the creditworthiness of counterparties. In addition to monitoring credit limits, the Group manages the credit exposure by entering into collateral arrangements with counterparties in appropriate circumstances, and limiting the duration of exposure. As per the private placement memorandum of the STS program, the Sukukholders bear the credit risk arising from investments.

Concentrations of credit risk arise when a number of counterparties are engaged in similar business activities, or activities in the same geographic region, or have similar economic features that would cause their ability to meet contractual obligations to be similarly affected by changes in economic, political or other conditions. Concentrations of credit risk indicate the relative sensitivity of the Group's performance to developments affecting a particular industry or geographic location. The Group seeks to manage its credit risk exposure through diversification of financing and investment activities to avoid undue concentrations of risks with individuals or groups of customers in specific locations or businesses.

The concentration of assets and liabilities is as below:

	2006		2005	
	<i>Assets</i> <i>US\$ 000's</i>	<i>Liabilities</i> <i>and equity</i> <i>US\$ 000's</i>	<i>Assets</i> <i>US\$ 000's</i>	<i>Liabilities</i> <i>and equity</i> <i>US\$ 000's</i>
Geographic region:				
Bahrain	88,197	69,679	61,708	41,517
Other GCC countries	131,914	150,432	43,645	63,836
	220,111	220,111	105,353	105,353
Industry sector:				
Banks and financial institutions	30,934	206,843	14,422	98,598
Government	48,053	-	24,752	-
Real estate	128,293	3,385	62,430	3,360
Others	12,831	9,883	3,749	3,395
	220,111	220,111	105,353	105,353

13 PROFIT SHARE RISK

This arises from the possibility that changes in the market profit margin will affect the value of financial instruments. The Bank monitors and adjusts its maturity structure to minimise the related risk.

As part of managing the STS Program the Bank is exposed to profit rate risk, since returns to Sukuk holders are based on a floating rate compared to return from certain investments in Sukuk at fixed rate.

14 CURRENCY RISK

The Group had no significant foreign currency exposures at the balance sheet date.

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15 SUKUK ASSETS UNDER MANAGEMENT

Sukuk assets under management are as follows:

	<i>2006</i> <i>US\$ 000's</i>	<i>2005</i> <i>US\$ 000's</i>
Proprietary	83,500	49,500
Clients	868,000	718,603
	951,500	768,103

The Bank acts as an agent for facilitating the sourcing and securitisation of assets. The proprietary assets are included in the consolidated balance sheet, while client assets, which are managed in fiduciary capacity without risk or recourse to the Bank, are not included in the consolidated balance sheet.

16 FAIR VALUE OF FINANCIAL INSTRUMENTS

Fair value is the amount for which an asset could be exchanged or a liability settled between knowledgeable and willing parties in an arm's length transaction. Consequently, differences can arise between carrying values and fair value estimates.

Included under investments are unquoted available for sale investments amounting to US\$ 4.85 million (2005: US\$ 4.15 million), which are carried at cost due to lack of suitable methods for arriving at a reliable fair value for these investments.

17 EARNINGS AND EXPENSES PROHIBITED BY SHARI'A

During the year there were no earnings realised by the Group from transactions which were not permitted by Shari'a.